Content of question:

Which excess of the real estate property value over the exposure amount is considered to be "a substantial margin" under the Standardised Approach?

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Piece of law	**Decree No. 123/2007 Coll. (as amended)**
Provision	**Annex 4, 9, A.c), 4**
Explanation	Neither valid EU legislation nor Czech legislation stipulates which excess can be regarded as a substantial margin. Therefore, the principles to be applied in a given situation are general principles for risk management laid down primarily in the Act on Banks and the Decree, which imply that the liable entity itself must have a clear policy regarding this matter. Subsequently, the supervisory authority inspects that this requirement is met. The condition of the substantial margin can also be fulfilled for a portion of the exposure only. The LTV ratio laid down for the purpose of the proper coverage of mortgage-backed bonds (this ratio may not exceed 70% pursuant to Art 30, para 1 of the Act on Bonds) or the collateralisation level required in the case of the IRB Approach pursuant to Annex 16 to the Decree (this level equals 140% of the exposure amount, which roughly corresponds to an LTV ratio of 70%) may serve as a supportive measure. This value should be applied to residential real estate property as a standard. However, a stricter LTV ratio should be required in the case of non-residential real estate property (in the case of covered bonds this ratio may not exceed 60%, or 70% in some particular instances). This issue has also been discussed at the EU level, namely in the working group dealing with the transposition of Directive 2006/48/EC (CRDTG question No. 148). However, the Commission's answer only states that the goal of the margin is to assure that the recovery value of the property is enough to cover the outstanding exposure if the obligor defaults, as the exposure should be fully and completely secured by the property. Such requirement can be considered to be met if, in determining the required amount of the margin, the liable entity has used, for example, historical data about proceeds from foreclosures (or, at a minimum, data about the volatility of prices), taking account of the current situation in the market. However, it is also necessary to take into consideration the individual features of the real estate property, for example, the purpose of its use or its location, and the time period needed for the foreclosure of a real estate property with similar features.